

Opportunity Cost Table		
	CLOTHING	AEROPLANE
US	$12/5=2.4$	$5/12=0.41$
BRAZIL	$1/4=0.25$	$4/1=4$

The above opportunity cost table shows that, the US has a comparative advantage in producing aeroplanes. This is because the opportunity cost of producing aeroplanes ($5/12=0.41$) is lower than that of Cloth ($12/5=2.4$) in US. Therefore, US should specialise in producing aeroplanes even though it has absolute advantage in both cloth and aeroplanes.

In contrast, Brazil has a comparative advantage in producing Cloth. Brazil produces clothing, the opportunity cost is $1/5 = 0.25$ aeroplanes as the one shown in above table. This is because the opportunity cost of producing cloth ($1/4=0.25$) is lower than that of aeroplanes ($4/1=4$) in Brazil. Therefore, Brazil should specialise in producing clothing even though it doesn't have an absolute advantage.

Therefore, we conclude that based on comparative cost advantage analysis, both US and Brazil will be benefited by trading each other.

Criticisms of the Theory

As with many other economic ideas, there are criticisms to be levelled at comparative cost advantage theory:

- (i) It is much more complicated in the real world in deciding in which goods countries have a comparative cost advantage. This is so because there are a large number of goods and many countries.
- (ii) The theory ignores the effects of transport costs. However, once transport costs are added any comparative advantage may be lost.
- (iii) Modern theories, no longer based on Ricardo's labour theory, have established that the only necessary condition for the possibility of gains from trade is that price ratios should differ between countries.
- (iv) Ricardo ignored the role of demand completely and explained trade from supply side.
- (v) Ricardo's analysis is based on the labour theory of value as costs are expressed in terms of labour hours. However, the classical labour theory itself has lost its relevance.
- (vi) The theory applied their principle in case of trade with two countries only and with two commodities only. So, the principle has a limited scope of application in practice. It cannot explain multi-lateral trade.